EXPLANATORY MEMORANDUM TO

THE CONTRACTS FOR DIFFERENCE (STANDARD TERMS) (AMENDMENT) REGULATIONS 2017

2017 No. 112

1. Introduction

1.1 This explanatory memorandum has been prepared by the Department for Business, Energy and Industrial Strategy and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

2.1 This instrument amends the Contracts for Difference (Standard Terms) Regulations 2014 (S.I. 2014/2012) (as amended) ("the 2014 Regulations") to enable the associated Contracts for Difference ("CFD") Standard Terms and Conditions ("Standard Terms") to set out when payments to generators under a CFD will not be made. The precise circumstances will be set out in the Standard Terms. The Standard Terms are published when issued or revised by the Secretary of State and are available on the government website.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

3.1 None.

Other matters of interest to the House of Commons

3.2 As this instrument is subject to the negative procedure and has not been prayed against, consideration as to whether there are other matters of interest to the House of Commons does not arise at this stage.

4. Legislative Context

4.1 The 2014 Regulations set out the provisions that must be included in the Standard Terms, including that where a strike price is higher than a reference price, the CFD counterparty must pay the generator the difference. There is currently a specific exception to this, to allow the Standard Terms to prevent payments being made to generators during periods of negative electricity prices.

4.2 Standard Terms were first issued in 2014 in advance of the first CFD allocation round. The government has consulted on proposed amendments to the Standard Terms in 2015 and 2016, and intends to publish revised Standard Terms in advance of the next CFD allocation round.

4.3 The government consulted on proposed amendments to the Standard Terms to avoid the cumulation of CFD payments with other forms of state aid. These proposals include permitting the CFD counterparty to set-off any other amounts of state aid against CFD payments, so that generators do not receive CFD payments until the other state aid has been deducted.

4.4 The amendments to the 2014 Regulations will allow Standard Terms to be published which set out circumstances in which difference payments are not required to be paid to the generator. This is intended to capture the state aid set-off situation described above, in addition to the negative electricity pricing scenario (and the specific negative pricing exception is accordingly removed, as no longer required). If in the future any further exceptions to the general principle are proposed, this amendment would enable those proposals to be implemented in the Standard Terms. The Secretary of State is required to consult before publishing revised Standard Terms.

5. Extent and Territorial Application

5.1 The extent of this instrument is the United Kingdom.

5.2 The territorial application of this instrument is the United Kingdom.

6. European Convention on Human Rights

6.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

7. Policy background

What is being done and why

7.1 CFDs are intended to incentivise investment in low carbon electricity generation, while improving affordability for consumers and maintaining energy security. CFDs are contracts between a low carbon electricity generator and a government-owned counterparty, the CFD counterparty.

7.2 Under the CFD, the CFD counterparty will pay the generator the difference between a fixed strike price and a reference price. If a reference price is higher than a strike price, the generator will pay the difference to the CFD counterparty. In this way, CFDs provide long term price stabilisation to low carbon generators, allowing investment to come forward at a lower cost of capital and a lower cost to consumers.

7.3 Whilst the general principle of the CFD is that generators will receive difference payments, there are some limited circumstances in which that is not the case, such as for example where a set-off is made to avoid state aid cumulation.

7.4 CFD payments are a form of state aid which has been approved by the European Commission. The government consulted on proposed amendments to the Standard Terms to prevent generators receiving CFD payments alongside other forms of state aid, in order to ensure there is no overcompensation and ensure compliance with the European Commission's state aid approval of the CFD scheme. The proposals include permitting the CFD counterparty to set-off any other amounts of state aid against CFD payments, so that generators do not receive their CFD payments until the other state aid has been deducted. The precise circumstances will be set out in the Standard Terms.

7.5 If in the future the government proposes further circumstances in which CFD payments will not be made, or not made in full, then this amendment would enable those changes to be implemented in the Standard Terms. The intention that the amendment would capture other circumstances which might be specified in the Standard Terms in future was consulted on. The Secretary of State is required to consult before publishing revised Standard Terms.

Consolidation

7.6 The department does not intend to consolidate the relevant legislation at this time.

8. Consultation outcome

8.1 The policy set out in this instrument was subject to a consultation ("Consultation on changes to the CFD contract and CFD regulations") from 11 May to 8 June 2016, which allowed stakeholders to provide feedback on this proposal and on the proposed amendments to the Standard Terms. The government felt it was appropriate to undertake a four-week consultation as the majority of the proposals were clarifying amendments of a minor and technical nature that are not fundamental to the CFD scheme, the largest of the changes was to ensure compliance with the state aid approval, and the changes concerned the existing CFD scheme which stakeholders were already actively engaged on.

8.2 Sixty two responses to the consultation were received. Respondents did not raise concerns with this proposed amendment and responses were focused on the proposed changes to the Standard Terms. The responses on the proposal to amend the Standard Terms to allow the CFD counterparty to set-off other state aid against CFD payments were supportive, with the majority of respondents (over 75%) who expressed an opinion supporting the proposal. Of those who disagreed, concerns were raised that deductions from CFD payments would have a negative impact on cash-flow. The government response to the consultation has been published[1] and summarises the views of stakeholders and sets out the final policy decisions taken in relation to the package of proposed amendments to the Standard Terms.

9. Guidance

9.1 Guidance is provided via Gov.uk, acting as a gateway to information on CFDs, regulatory amendments and links to information provided by delivery partners.

9.2 Further details are also available in the government response to the consultation, which has been published to coincide with the laying of the regulations in Parliament. The government response sets out the views of stakeholders and provides an explanation of the final policy decisions taken in relation to the package of proposed amendments to the Standard Terms.

10. Impact

10.1 The impact on business, charities or voluntary bodies is negligible. These Regulations impact only on generators who choose to apply for a CFD (and are successful) in respect of an eligible generating station. Applying for a CFD is voluntary.

10.2 There is no impact on the public sector.

10.3 An Impact Assessment is available and published alongside the Explanatory Memorandum for the 2014 Regulations on the legislation.gov.uk website. The Impact Assessment refers to the wider CFD regime. The amendment brought about by these regulations is minor and the impact is not expected to alter the balance of costs and benefits discussed in the Impact Assessment.

[1] https://www.gov.uk/government/consultations/consultation-on-amending-the-cfd-contract-and-regulations

11. Regulating small business

11.1 The legislation applies to activities that are undertaken by small businesses, who are free to apply for a CFD if they are building an eligible generating station.

11.2 However, regulation 14 of the Contracts for Difference (Allocation) Regulations 2014 (as amended) provides that there are types of application for a CFD which are excluded from Parts 2 to 9 of those Regulations, including where the small scale Feed-in Tariff is available for the generating station, such as onshore wind, hydro, solar PV or anaerobic digestion generation of less than or equal to 5MW.

11.3 The department has sought to consult as widely as possible to ensure the views of stakeholders have been taken into account in the development of CFDs.

12. Monitoring & review

12.1 Section 5(4) of the Energy Act 2013 requires the Secretary of State to prepare and lay before Parliament a report setting out how the Secretary of State has carried out his Electricity Market Reform (EMR) functions. The section requires the Secretary of State to report, before 31 December each year and beginning in 2014, on how he has carried out his functions in Part 2 of the Act in order to deliver EMR's objectives. The report must be laid in Parliament and be shared with the Devolved Administrations. As well as fulfilling the reporting requirement, the EMR Annual Update provides Parliament and other stakeholders with a forward look of the path ahead and a summary of EMR progress since the Energy Bill received Royal Assent in December 2013.

12.2 In addition, section 66 of the Energy Act 2013, requires the Secretary of State to report to Parliament by the end of 2018 on a number of aspects of the operation of the EMR programme. These aspects include the extent to which the original objectives have been met, whether these objectives are still appropriate and whether they could be delivered in a way that imposes less regulation.

13. Contact

13.1 Kieran Power at the Department for Business, Energy and Industrial Strategy Telephone: 0300 068 6189 or email: kieran.power@beis.gov.uk can answer any queries regarding the instrument.